Nos. 226, 227, 243

IN THE

Supreme Court of the United States

OCTOBER TERM, 1948

No. 226

SECURITIES AND EXCHANGE COMMISSION,
Petitioner,

v.

CENTRAL-ILLINOIS SECURITIES CORPORATION, C. A. JOHNSON, LUCILLE WHITE and FRANCES BOEHM.

No. 227

THOMAS W. STREETER, et al.,
Petitioners,

v.

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No. 243

THE HOME INSURANCE COMPANY and TRADESMAN'S NATIONAL BANK AND TRUST COMPANY,
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ON PETITIONS FOR WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF RESPONDENTS CENTRAL-ILLINOIS SECURITIES CORPORATION AND CHRISTIAN A. JOHNSON, IN OPPOSITION

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Opinions Below

The opinion and judgment of the Court below (R. 12) and the opinion denying petitions and cross-petitions for rehearings (R. 138) are reported at 168 F. 2d 722. The

opinion of the District Court is reported at 71 F. Supp. 797 (R. 283a), but its detailed Findings of Fact and Conclusions of Law (R. 293a-317a) are not reported. The Findings and Opinions of the Commission dated December 4, 1946 and January 8, 1947 have not yet been officially reported but are set forth in the Commission's Holding Company Act Releases Nos. 7041 (R. 25a) and 7119 (R. 128a).

Jurisdiction

The judgment of the Circuit Court of Appeals for the Third Circuit was entered March 19, 1948, and its judgment denying petitions and cross-petitions for rehearing was entered June 11, 1948. The jurisdiction of this Court is invoked under Section 240 of the Judicial Code, as amended by the Act of February 13, 1925 (28 U. S. C. 347), made applicable by Section 25 of the Public Utility Holding Company Act of 1935, 49 Stat. 803 (15 U. S. C. 79 *et seq.*).

Statute Involved

The provisions of Sections 11(e) and 24(a) of the Public Utility Holding Company Act of 1935, 49 Stat. 803, 15 U. S. C. 79a, *et seq.*, are set forth in the Appendix, *infra*, pp. 37-38.

Questions Presented

1. Where a federal statute compels the complete and final termination of a holding company system and of the investments of all security holders therein, are the common stockholders required to indemnify the preferred stockholders against the possibility that upon reinvestment of their funds elsewhere the latter may receive dividends at the somewhat lower rates then current?

2. Was the District Court, in performing its statutory duties under Section 11(e) of the Public Utility Holding Company Act, required to accept the Securities and Exchange Commission's interpretative legal conclusions: (a) disregarding well-settled judicial principles held applicable by the Commission and numerous courts to forced retirement under the Act of senior securities, and (b) fictionally "measuring the rights" of the preferred stockholders (but not of the common stockholders) "as though in a continuing enterprise", even though incontrovertibly the entire enterprise has come to an end?

3. Were the District Court and the Circuit Court of Appeals, in performing their respective functions, required to accept as conclusive of the rights of all security holders in a final liquidation a finding by the Commission of the "value" of the preferred stocks based merely on their hypothetical market price as of a given moment "apart from the impact of liquidation under Section 11", and in disregard of all the other impacts of the statute and their vital bearing on such "value"?

Statement

In our cross-petition heretofore filed,[1] there is set forth a comprehensive Statement of the Case, which we respectfully request be deemed incorporated herein by reference in order to avoid unnecessary duplication.

Notwithstanding the hardship which the additional delay and expense will impose on the common stockholders,[2] we

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[1] *Central-Illinois Securities Corporation and Christian A. Johnson, Petitioners* v. *Securities and Exchange Commission, Thomas W. Streeter, et al., The Home Insurance Co., et al.*, No. 266, October Term, 1948. The earlier date required for filing of the cross-petition rendered unfeasible its joinder with this brief, but the two documents are intended to be supplementary to one another.

[2] Under the Commission's decision, all expenses and costs in connection with all phases of the proceedings and litigation relating to the plan must be borne by the common stockholders (R. 72a-82a).

would not question the desirability of review by this Court if the Commission's decision in this case threatened to set a pattern for future decisions in dissolutions under the Holding Company Act; but we venture to suggest that as a practical matter the sharp upward revisions in money rates generally and in public utility preferred stock yields in particular have rendered the principal questions raised by the petitions virtually moot, not alone for the time being but for the foreseeable future.

However reluctant the Commission may be to face the fact, the "investment value ex the Act" doctrine has been swept away with the temporary war's-end stock market boom which engendered it. This factor, even apart from the basic fallacies in the doctrine pointed out by the two Courts below, which respectively have had more judicial experience with orders and plans under Section 11 than any other District and Circuit Courts in the country,[3] and which have hitherto consistently upheld the Commission's determinations, strongly supports the view that the issues precipitated by the Commission's decision in this case are not likely to prove recurrent, and certainly not in the form here presented.

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[3] See Circuit Court's opinion (R. 30, 39) for compilation of more than twenty-seven Section 11 decisions by District Judge Leahy. See also the following Section 11 decisions by the Third Circuit Court of Appeals:

Commonwealth & Southern Corp. v. S. E. C., 134 F. 2d 747; *United Gas Improvement Co.* v. *S. E. C.*, 138 F. 2d 1010; *In re Securities & Exchange Commission (Otis & Co.)*, 142 F. 2d 411, aff'd *sub nom. Otis & Co.* v. *S. E. C.*, 323 U. S. 624; *Lownsbury* v. *S. E. C.*, 151 F. 2d 217, *cert. den.* 326 U. S. 782; *In the Matter of Standard Gas & Electric Co.*, 151 F. 2d 326; *In the Matter of United Gas Corp.*, 162 F. 2d 409; *In the Matter of Community Gas & Power*, 168 F. 2d 741, *cert. den.* 334 U. S. 846. See also decision of Judge Biggs in *Re Midland United Co.*, 58 F. Supp. 667.

ARGUMENT

I. REVIEW OF THE CIRCUIT COURT'S ORDER AS REQUESTED BY PETITIONERS IS NOT PRESENTLY APPROPRIATE.

We are confronted at the outset with the crucial and authoritative data presented to the Circuit Court and included in the present record (R. 122-123) which establishes that the Engineers preferred stocks if presently outstanding would have an "investment value" (employing this term in the very sense used by the Commission) not in excess of $90-$95 per share. In its application to the instant case, therefore, this changed "value" *of itself* is decisive of the only ultimate issue; viz., whether the preferred stockholders are entitled to receive amounts in excess of the $100 per share plus dividends already paid to them. Consequently, even if this Court found it possible to uphold the Commission's "investment ex the Act" doctrine as applied in this case, and were also to hold that the Courts below were wrong on every issue, no additional amounts could be found payable to the preferred stockholders on the basis of the Commission's own rationale and formula for which Petitioners here contend.[4]

[4] It is beyond dispute that the changes in applicable money rates and yields which occurred subsequent to the issuance of the Commission's opinions have a crucial bearing on "investment values" as determined in this case by the Commission. A final decree cannot be entered without consideration of these vital changed factors, since the decree of a court of equity speaks "as of the date of entry" and must therefore take account of all material changes which have occurred since the commencement of the proceedings: *Randel* v. *Brown*, 2 How. 405, 422; *McCabe* v. *Guaranty Trust Co.*, 243 Fed. 845, 849; *Brooks Bros.* v. *Brooks Clothing Co. of California*, 60 F. Supp. 442, 456; *Knight* v. *Wertheim & Co.*, 158 F. 2d 883, *cert. den. sub. nom. McGuire* v. *Equitable Office Bldg. Corp.*, 331 U. S. 818. Nor is there any basis for a contention that these changes had been envisaged and taken into account by the Commission; concurrent findings of both Courts below incontrovertibly establish that the Commission's determination was based merely on "values" as of May, 1946 and that

If this vital factor does not render the case technically moot, it at least renders it "unripe" for review here in the light of the character of the Circuit Court's order. That order did not, by its terms, finally determine the rights of any of the parties to these proceedings, but instead remanded the proceedings to the Commission for further consideration of factors relating to the valuation of the preferreds and the common (R. 39-40). The remand will also afford opportunity for appropriate consideration of the impact of the changed money rates. These are questions which properly should be determined before this Court is called upon to pass on underlying issues of law which, we submit, will become academic in the light of such factual determinations; cf. *Republic Natural Gas Co.* v. *State of Oklahoma*, 334 U. S. 62.[5]

Apart from the untimeliness of review now, we also submit that on the merits the decision below is entirely correct, except in requiring remand of the proceedings to the Commission. This latter requirement, although fraught

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no consideration whatever was given to future trends or possible changes (Circuit Court, R. 17; District Court, R. 310a-315a).

In a more recent opinion the Commission itself stated concerning "investment values" determined as of this very period:

> "* * * the Commission's findings were issued in May of 1946 *in what has since proven to be the peak of the post-war market.* The market has declined substantially from the highs reached at that time and there has been a material firming of interest and preferred yields. It is apparent that insofar as investment value is derived from an analysis of the current yields of comparable securities, *the investment value of American's preferred has been substantially affected in the interim.* In addition, there have of course been changes in the financial and business aspects of the company which have a direct bearing on the value of the security" *(United Light and Railways Co.—American Light & Traction Co.*, Holding Company Act Release No. 7951, p. 33, Dec. 31, 1947; emphasis supplied.

[5] This decision, though dealing with "finality" of the judgment of a state court, contains reasoning wholly applicable to the instant case. See also *Robertson and Kirkham, Jurisdiction of the Supreme Court* [1936], Section 116, for the proposition that ordinarily the writ will not issue to review a judgment of the Circuit Court of Appeals unless it is final.

with substantial prejudice to respondents for the reasons set forth in our cross-petition, represents in essence an act of deference to Petitioner Securities and Exchange Commission, of which surely Petitioners have no valid cause to complain, since under the circumstances of this case the Circuit Court should have wholly affirmed the District Court's decree.[6] The threat of complexities and uncertainties in the administration of the Act which Petitioners profess to find lurking in certain phrases of the opinion below will be found, upon examination, to reflect primarily subtle exaggerations of portions of the Circuit Court's language. Similarly, the asserted conflict among the Circuits will be found actually non-existent.

II. THE CIRCUIT COURT CORRECTLY HELD THAT THE DISTRICT COURT UNDER SECTION 11(e) IS NOT A MERE "REVIEW COURT". THERE IS NO CONFLICT AMONG THE CIRCUITS:

Despite their emphatic assertions that the Circuit Court erred in interpreting the functions of the District Court under Section 11(e), it is significant that Petitioners have not even ventured to join issue with the Court's detailed and searching analysis of the pertinent statutory provisions (R. 24-34). Nor have Petitioners found it possible to throw any different light on the legislative history, painstakingly marshalled and set forth by the Court (R. 21-24), establishing beyond doubt that Congress intended with respect to Section 11(e) plans affecting stockholders' rights that the traditional powers of the District Court as an equity reorganization tribunal should not be materially "diminished or encroached upon by the functions allotted to the Commission under the law" (R. 22); and that the role of the Commission with respect to plans requiring judicial enforcement under Section 11(e) was envisaged primarily as

[6] See discussion at pp. 24-30 of our cross-petition (No. 266).

that of "expert economic adviser and administrative assistant" to the Courts (R. 22), as compared with the broader role confided to the Commission under the numerous other provisions of the Act.[7]

Indeed the Commission's petition asserts (p. 22) that the Commission is in agreement with much of what the Circuit Court stated as to the independent role of the District Court, a position markedly different from that which it took before the Circuit Court, but more consistent with the views which it has repeatedly expressed in its reports to Congress and testimony before Congressional Committees to which the Court's opinion makes pointed reference (R. 23, 30). But having made this strategic obeisance to its own recorded statements, the Commission proceeds to urge in effect that the District Court's "independent" judgment may be employed to approve, but never to disapprove, the Commission's conclusions; in short, the District Court's "independence" must always end at the precise point where disagreement with the Commission begins.

The Commission seeks to accomplish this result by requesting this Court to drastically amend the statute in order to *ingraft* the substantial evidence rule embodied in Section 24(a) upon Section 11(e), so as to make the findings of the Commission binding upon the District Court if supported by evidence. Even if it were possible to disregard the violence to the statutory scheme and fixed Congressional purpose pointed to by the Circuit Court, such an

[7] There is an obvious and clear distinction in the statutory scheme between Sections 11(d) and (e) and the remaining sections of the Act. The latter embody the fundamental regulatory and administrative functions of the Commission; as to which its judgment was intended to have the full scope normally confided to administrative agencies. Sections 11(d) and (e), on the other hand, constitute in effect a "self-contained reorganization statute" (as the Commission itself has stated, note 11, *infra*) which is merely *ancillary* to effectuation of the primary statutory objectives embodied in Section 11(b), and which relies on the traditional powers and expert techniques of the District Courts as equity reorganization and anti-trust tribunals (Cf. Circuit Court Opinion, R. 21-23).

amendment would not aid Petitioners' position in the instant case. For the findings of the Commission which Section 24(a) states shall be conclusive if supported by substantial evidence, are "findings *as to the facts*". There is no contention here, and there could not be, that the factual findings of the Commission were contravened by those of the District Judge, particularly since almost all the facts recited by the latter (and fully affirmed by the Circuit Court[8]) are also referred to in the Commission's findings and opinions. The conflict between the District Court and the Commission related primarily to the *legal conclusions* to be drawn from those facts.[9]

Recognizing this, Petitioners are compelled to the further and even more drastic contention that the enforcement court must similarly be bound by the Commission's *legal conclusions*. But even this extreme position would not enable Petitioners to prevail in the instant case because the "essence of the holdings of both Courts below was that the Commission's *conclusions* are without substantial evidentiary or legal basis; or, stated in the restrictive terms for which Petitioners contend, that they "lack rational or statutory foundation".

That such holdings of the Courts are correct, and in fact unassailable, will be demonstrated in subsequent portions of this brief. Initially, however, it must be observed how feeble is the reed on which Petitioners are obliged to hang their momentous argument for judicially fusing Sections 11(e) and 24(a). It is significant that the sole deci-

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[8] With respect to the weight which attaches in this Court to the concurrent findings of two Courts below, see *Comstock* v. *Group of Institutional Investors*, 335 U. S. 211, 214, and decisions there collated.

[9] We assume that questions of nomenclature are not properly to be deemed questions of fact. Thus, although the District Judge accepted the Commission's finding that the preferred stocks had a "value" as of May, 1946, as found by the Commission, he was unable to accept the descriptive title "investment value ex the Act" for values which were primarily transient *market* values as of a particular moment. (See discussion *infra*, pp. 21-24.)

sion to which the Commission refers for support of this proposition is an unreported case in the District Court of Delaware dating back to the early stages of Section 11(e) programs, and that the Commission has failed to explain why this is, as it admits, "the only instance" of its kind.[10] Moreover, the Commission has not called to the Court's attention the more recent and authoritative decisions throwing a very different light on the subject. We refer to *Okin* v. *S. E. C.*, 145 F. 2d 206 (C. C. A. 2, 1944), remanded 325 U. S. 840, and *Lownsbury* v. *S. E. C.*, 151 F. 217 (C. C. A. 3, 1945), *cert. den.* 326 U. S. 872, where the Commission urged upon the Courts that "the statutory scheme renders inapplicable the general review provisions of Section 24(a)" with respect to Section 11(e) plans cutting across stockholders' charter rights; that in recognition of this statutory scheme the Commission has established the practice of expressly conditioning its approval of such plans upon District Court enforcement; and that Circuit Courts of Appeal wholly lack jurisdiction under Section 24(a) to review such Commission orders.[11]

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[10] See Commission Petition, p. 24, note 11. In its brief in this Court in *Okin* v. *S. E. C.*, 325 U. S. 840 (No. 601, October Term, 1945), the Commission had occasion to explain (p. 14, note 9) the extraordinary circumstances under which this case arose.

[11] Thus, in its brief in this Court in opposition to certiorari in the *Lownsbury* case, *supra* (No. 1245, October Term, 1944), the Commission stated:

> "Congress contemplated that reorganization techniques should be available for compliance with Section 11(b) orders, and subsections (d) and (e) are in many respects a self-contained reorganization statute with provisions defining the respective reorganization functions of court and agency which are comparable to the relationship between the Interstate Commerce Commission and the courts prescribed in the previously enacted Section 77 of the Bankruptcy Act. Section 11(f) provides for a similar allocation of function as between the Commission and a reorganization court where the court's reorganization jurisdiction stems from sources other than the Holding Company Act" (p. 7).
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> * * * * * *
>
> "An order of the Commission approving the plan, which is to be operative only if subsequently approved by a district

Having successfully urged these views upon the Second and Third Circuits, and upon this Court in its briefs in opposition to certiorari, it scarcely seems admissible for the Commission to now argue that Sections 24(a) and 11(e) are merely "alternative ways" of reviewing Section 11(e) plans expressly conditioned, as was Engineers', upon District Court approval and enforcement; and that "the substantial evidence rule" of Section 24(a) should be forcibly propelled into Section 11(e), which the Commission previously urged is "a *self-contained* reorganization statute", and orders of the Commission thereunder "stand on an entirely different footing from the ordinary order of the Commission for which the review provisions of Section 24(a) were evidently intended".[12]

Even wholly apart from these inconsistencies, the Commission's argument is clearly devoid of merit. A Circuit Court of Appeals reviewing a Commission order under Section 24(a) is not called upon to enter its own decree as a court of equity enforcing a plan upon all security holders without their consent. A District Court under Section 77(e) of the Bankruptcy Act (which the Commission's petition *asserts* performs a statutory role "in general similar" to that of a Section 11(e) Court[13]) can scarcely be thought to function as a mere "review" court. Certainly, support for such a view cannot be derived from the decisions of this Court under Section 77(e) of the Bankruptcy Act, in which the Court has distinguished carefully between its own role as a review court and the wholly different role of the District Court, stating, for example:

> "* * * Since such a determination rests in the realm of judgment rather than mathematics, there

court pursuant to subsections (d) and (e) or under some independent source of jurisdiction recognized in subsection (f), stands on an entirely different footing from the ordinary order of the Commission for which the review provisions of Section 24(a) were evidently intended. * * *" (p. 9).

[12] Cf. note 11, *supra*.

[13] Commission petition, p. 22.

> is an area for disagreement. *But we are not performing the functions of the District Court under Section 77(e). Our role on review is a limited one.* It is not enough to reverse the District Court that we might have appraised the facts somewhat differently. If there is warrant for the action of the District Court, our task on review is at an end."[14] (Emphasis supplied.)

The spectre which Petitioners seek to conjure up with respect to the possibility of "stalemates" between the Commission and the District Courts (a spectre even more applicable to other reorganization statutes)[15] derives no substance from the Commission's experience with Section 11(e) plans in the Courts either prior to or subsequent to the decision in the instant case.[16] On the contrary, it

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[14] *Group of Institutional Investors* v. *Milwaukee R. R. Co.*, 318 U. S. 523, 564. See also the recognition accorded in *Comstock* v. *Group of Institutional Investors*, 335 U. S. 211, in both the majority opinion (p. 227) and that of the minority (p. 236) to the special functions of the district courts under Section 77(e).

[15] Thus, plans under Section 77 of the Bankruptcy Act not only require the approval of the Interstate Commerce Commission and the District Court, but also of every class of security holders affected. Such security holder approval is also required with respect to plans under Section X of the Bankruptcy Act, where the Commission also plays an active role and frequently carries to the appellate courts for review decisions of the district courts in conflict with the Commission's views. Cf. *S. E. C.* v. *U. S. Realty & Improvement Co.*, 310 U. S. 434.

[16] It is pointed out in the opinion of the Circuit Court that the Commission had submitted some sixty-three Section 11(e) plans to the District Courts for enforcement, all of which have been carried out, and that Judge Leahy had passed upon twenty-seven of those plans. Subsequent to the Circuit Court's decision in the instant case Judge Leahy has passed on nine additional Section 11(e) plans, all of which he has approved and enforced. Prior to the *Engineers* decision, in fulfilling his "independent duty" Judge Leahy had concurred in the conclusions of the Commission in every plan presented to him with the sole exception of a single phase of one plan. The Third Circuit reversed, holding that since the question related to the "appropriateness" of the "particular remedial measures" required to effectuate Section 11(b), the Commission's judgment

is very plain that the danger is less that the District Courts will seek to usurp the Commission's functions than that they will tend to abdicate their own.

This is demonstrated by the very decisions to which Petitioners point as establishing a "conflict among the circuits" in relation to the instant case.[17] Such conflict does not in fact exist. Those decisions involved appeals to Circuit Courts from decrees of district courts which *approved and enforced* Section 11(e) plans previously also approved by the Commission. Thus, the Circuit Courts were in each instance reviewing plans bearing the *concurrent approval of both* the District Court and the Commission, and the Circuit Courts' opinions refer repeatedly to the findings of the Court below as well as to those of the Commission. The specific language in the opinions as to the weight to be attributed to the Commission's findings[18] has reference to the complaints of the appellants that the District Judges had "abdicated" their statutory duties by accepting the Commission's findings and determinations without according them an adequate independent check. The holdings of the appellate courts that the district courts were *entitled* in the exercise of their discretion to attach great weight to the Commission's findings obviously cannot be construed as holdings that the district courts are *required* in performing their statutory functions to ap-

should prevail (*In re Standard Gas & Electric Co.*, 151 F. 2d 326, 331). However, subsequent events established the correctness of the District Judge's fears that fluctuating markets would render the plan unfair; and as a result the Commission itself concurred in the view that the claims of the senior security holders should be discharged in cash. (See *In re Standard Gas & Electric Co.*, 63 F. Supp. 876.)

[17] Commission petition, p. 21; Streeter petition, pp. 17-20.

[18] Petitioners place great emphasis on the statement of the Circuit Court in the instant case that the cited decisions "look the other way" (R. 31). It is evident that the Circuit Court's statement was made on the basis of the quotations from the cited opinions set forth in Petitioners' briefs, rather than an independent analysis of the decisions themselves.

prove and enforce determinations of the Commission which they deem erroneous.[19]

In the instant case the Circuit Court went very far in enjoining upon the district courts the limitations of their statutory role, emphasizing that such courts may not substitute their own values or estimates for those of the Commission, nor "act capriciously in rejecting valuations made by the Commission" (R. 34, 39).[20] Indeed, as is indicated by our cross-petition, we believe it went too far in applying these principles in the particular context of this case. Subject only to this exception, we submit that the Circuit Court's conclusions as to the respective functions of the district courts and the Commission are not only unassailable on the basis of statutory analysis and legislative history, but, contrary to Petitioners' suggestions, their effects will prove highly salutary.[21] By contrast,

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[19] Moreover, it is to be noted that in the cases referred to by Petitioners the determinations accepted by the District Court, and of which appellants complained, related largely to such involved factual issues as the normal prospective earning power for the reorganized enterprise, and were thus questions of entirely different import from those on which the District Court and the Commission differed in the instant case.

[20] Cf. *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 279, quoted at p. 19 (note 18) of our cross-petition.

[21] The beneficial effect of this decision in its practical operation is evidenced by the recent decision of the District Court of Minnesota, *In the Matter of Northern States Power Company*, decided August 30, 1948. Holding that the Circuit Court's decision in the *Engineers* case did not preclude him from attaching great weight to the Commission's determinations as to earning power and allocation, the District Judge fully upheld them; but only after making a careful check of their correctness in the exercise of his "independent duty". The same course was followed, and the same result was reached, by the District Court of Maine, *In the Matter of American & Foreign Power Company*, decided September 16, 1948.

The fact is that there has not been a single instance of a refusal by a District Court to approve and enforce a Section 11(e) plan, or any portion thereof, since the decision in the instant case.

Petitioners' contentions would effectually strip security holders of a highly important portion of the protection which this Court has asserted they are assured under the statute, stating:

> "Any plan of divestment or reorganization, moreover, must be carefully scrutinized by *both* the Commission and the enforcing court, *thus enabling the assertion and protection of all shareholders' rights.*" *North American Co.* v. *S. E. C.*, 327 U. S. 686, 709. (Emphasis supplied.)

III. THE DECISION BELOW WAS WHOLLY CORRECT ON THE MERITS.

A. The Commission's rationale lacked legal, equitable or rational foundation.

(1) It is important at the outset to fix firmly in mind the Commission's rationale in holding that the Engineers' preferred stockholders were entitled to receive the redemption prices, aggregating $3,200,000 in excess of the liquidation preferences specified in the corporate charter. The Commission did not find, or even suggest, that the retirement of the preferred stocks constituted in letter or spirit a call and redemption within the purview of the redemption provisions of the charter. Instead, it found that the complete and final liquidation of the Engineers' enterprise was necessitated by the Act, and was involuntary. This is conceded by the Commission's petition (p. 9), which further concedes that a long line of Commission and court decisions uniformly hold that redemption premiums may not be claimed or paid under such circumstances in consonance with the "fair and equitable" standard of Section 11(e) (see cases cited at p. 9, note 2, of Commission's petition).

The Commission held that the redemption premiums should be paid on the Engineers' preferreds solely because the dividend rates of these stocks were in excess of the

then prevailing preferred stock yields and money rates and for that reason the stocks would have had a "value" approximating the redemption prices *if* the Act had not compelled the retirement of the preferred stocks and the dissolution of the enterprise. We defer for the moment discussion of the significance of this admittedly fictional hypothesis in order to examine the asserted "values". Initially it is to be observed that the very same "value" factor was also present in most of the non-premium cases cited by the Commission at page 9 of its petition, and was invariably held irrelevant by the Commission and the courts. Thus, in the leading case in which the non-premium principle was enunciated, the Commission had squarely before it the contention of debenture holders that wholly apart from any contractual rights to the redemption premiums [22] they should as a matter of "fairness and equity" receive amounts in excess of the face amount of their bonds because they were being deprived prematurely of a valuable investment bearing interest rates of 6% and 6½%, rates so lucrative that the debentures had been selling at *a premium above par* despite the imminence of retirement. The Commission replied to this contention as follows:

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[22] In rejecting the claim of the debenture holders that they were entitled to the redemption premiums under the terms of the indenture, the Commission stated:

> "We believe that the obligation to pay a premium was intended to arise only when the company was to continue as a going concern, for the payment thereof is in the nature of compensation payable by the company (i.e., its stockholders) to the debenture holders for depriving the latter of their investment. In a going concern, the stockholders may be deemed to benefit from the elimination or reduction of the debt effected by the redemption, and the premium may be regarded as the prearranged amount payable by them for such benefit.
>
> "But here the company does not continue as a going concern. There is no question of free choice or election. The company by virtue of congressional mandate is to terminate its existence. Power must liquidate not only its debt but its stock. The rights of debenture holders and stockholders alike to retain their respective investments, are cut off" (*The United Light & Power Company*, 10 S. E. C. 1215, 1221).

"It seems to us *a complete answer* to this argument that the termination of the investments of debenture holders and stockholders alike has been brought about by the act of a sovereign power—in this case a congressional mandate. We think the debenture holders have established no right to receive such compensation here at the expense of the stockholders, whose rights we must also consider." *The United Light & Power Co.*, 10 S. E. C. 1215, 1228. (Emphasis supplied.)

On appeal, the Second Circuit affirmed the Commission's order, holding that the doctrine of frustration of the enterprise was applicable.[23] Thereafter, this doctrine was consistently applied by the Commission and the courts in the numerous cases involving retirements of bonds and preferred stocks of holding companies required to liquidate in whole, or merely in part.[24] In virtually all these cases the securities had dividend or interest rates and an investment caliber as high or higher than those of the Engineers' preferreds. It was similarly contended that by reason of the prevailing low money rates these securities would have a "value" in excess of their par or stated amount if they had been permitted to remain outstanding; indeed, many had actually been selling at substantial premiums. It was found, however, "a complete answer" that the retirement of the securities was compelled "by Act of the Sovereign", and that the asserted deprivations were "consequential".[25]

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[23] *New York Trust Co.* v. *S. E. C.*, 131 F. 2d 274, cert. den. 318 U. S. 786, rehearing den. 319 U. S. 781.

[24] Not less than four different Circuit Courts of Appeals and many District Courts have passed on the question and have uniformly held the premiums not payable; the cases are collated at note 21 (p. 21) of our cross-petition.

[25] Cf. *The United Light & Power Co.*, 10 S. E. C. 1215 (quoted *supra*); *New York Trust Co. v. S. E. C.*, *supra*. See also the decision of Judge Leahy approving and enforcing the Commission's decision in *Consolidated Electric & Gas Co.*, 55 F. Supp. 211, 215.

Nor can it be urged that the validity of these decisions was in any way affected by the *Otis* decision, since two of the non-premium decisions are there cited with approval (323 U. S. 624, 638), and many non-premium decisions have been rendered by the Commission and the Courts subsequent thereto.

It is a curious and anomalous circumstance that in applying the Commission's new "investment ex the Act" doctrine to require premiums to be paid to the Engineers preferreds the Commission's findings and opinions in the instant case avoided even the slightest reference to the long and deeply-rooted series of decisions discussed above. Granting *arguendo* that the Commission is not bound by the doctrine of *stare decisis* or by its consistent administrative interpretation [26] of the "fair and equitable" standard of Section 11(e) for which over a four-year period it repeatedly asked and unfailingly received full judicial approval, there remained for the Courts below at the very least (even on the basis of the restrictive "review" standard for which petitioners contend) the duty of determining whether the Commission's new "investment value ex the Act" as here applied was compatible with established legal principles and the statutory intent. The Courts' conclusions that this issue must be determined in the negative were, we submit, virtually ineluctable.

Let it be assumed for purposes of the present discussion that, contrary to our firm contention, the liquidation provisions of the Engineers charter are not "controlling" in this liquidation,[27] and indeed that they may even be ignored as completely as the Commission ignored them. The problem of what shall take place when an enterprise is frustrated by governmental action, or by other super-

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[26] We presume that the doctrine of "consistent contemporaneous construction" is invoked only to uphold statutory interpretations by administrative agencies (Cf. *U. S.* v. *American Trucking Associations*, 310 U. S. 534, 549), but not to challenge them.

[27] As is stated more fully in our cross-petition in No. 266 (p. 27, note 31), we continue to maintain that these charter provisions are in fact controlling in respect of the type of final liquidation which both Courts below have found has here taken place; that the pertinent provisions of the Engineers charter are significantly different from those considered in *Otis* and are wholly applicable to this liquidation; that their overriding is not reasonably necessary to the effectuation of the fundamental Congressional objectives in enacting the Statute, and is violative of the Fifth Amendment of the Constitution.

vening events not contemplated by the parties, had been the subject of searching inquiry and repeated adjudication in the courts for decades prior to passage of the Holding Company Act.[28] The essence of these adjudications has been authoritatively formulated as follows:

> "Since there is no fault on either side, the loss due to impossibility or frustration must lie where it falls. *Neither party can be compelled to pay for the other's disappointed expectations.*"[29] (Emphasis supplied.)

The Commission's new doctrine is the very antithesis of this principle, for it holds that the common stockholders must compensate the senior security holders for the future deprivation of the high dividend rate which the latter have been receiving, even though admittedly this termination is caused wholly and directly by an Act of Congress passed to "effectuate an overriding public policy" (*Otis & Co.* v. *S. E. C.*, 323 U. S. 624, 637). It is not disputed that as of the moment of liquidation the preferred stockholders had received every dollar of dividends at the full rate stipulated in the charter, and that the cash payment of $100 per share returned to such holders the *maximum* amount which they or their predecessors had paid into the enterprise.[30] But it is contended (and the Commission

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[28] See 6 *Williston on Contracts* (Revised Edition, 1938), Section 1938 *et seq.*

[29] American Law Institute, *Restatement of the Law of Contracts*, Section 468 (comment on sub-section 3, p. 887).

More than forty years before enactment of the statute, the doctrine of frustration of the enterprise had been held determinative of the rights of stockholders of a corporation dissolved by compulsion of law (*Lorillard* v. *Clyde*, 142 N. Y. 446); and as has been indicated above, from the time of the earliest cases under the Holding Company Act the Commission and the courts recognized the applicability of this doctrine.

[30] Two of the issues were sold to the public at the time of issuance for $100 per share, and the third at $99.50 per share, although the company actually received on the average something less than $96 per share for all three issues. The $5 series carried the privilege of conversion until 1938 into common stock, a feature which

held) that simply because the preferred stockholders upon reinvestment in allegedly comparable preferred stocks might henceforth receive dividends at a somewhat lower rate based on the then current money rates, the common stockholders must *indemnify* the preferred for the future deprivation of their more desirable dividend rate despite the fact that this deprivation was compelled by the very federal statute which had also decreed liquidation of the entire enterprise and mandatory termination of the investments of all stockholders. Such a contention does not seem to us, any more than it did to the Courts below,[31] to rest on

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obviously had substantial value independently of the preferred (large amounts of this stock were converted into common at an average price of $52 per share in 1928-1929, a period where the common sold as high as $79¾). The $5.50 series (sold to the public at $99.50 per share) carried a warrant giving the holder a "call" on common stock over a 10-year period (District Court Finding No. 22, R. 301a). It is thus evident that in paying approximately $100 the original purchasers of these stocks were paying something *less* than $100 for the stock alone, since the conversion features and warrants had substantial value in their own right.

As to those who purchased subsequent to the initial issue, it is to be noted that the market price of all three issues from date of issuance until virtually the date of retirement ranged between $63-67, *averaged over the entire period* (Commission's opinion, R. 62a-63a). The record establishes that turnover during the period of depressed prices (particularly during the years when the preferreds were selling in the range of $10-$15 per share) was extremely heavy. Over the entire period, the turnover ratio of the $5 series was 335%; of the $5.50 series, 215%; of the $6 series, 195% (see Engineers Exs. 26-28, R. 1391a-1393a).

[31] "The preferred stockholders will receive every dollar which the common contracted to pay them, with the result that the preferred will have gotten back approximately $190 for every $100 which they, or their predecessors, initially invested in the enterprise. *But fairness and equity do not require that the preferred stockholders be paid an additional $3,200,000 for the theoretical future deprivation of their excessive dividend rate* * * *. In short, there is no reason why the preferreds should get additional compensation for the termination of the lucrative dividend rate which the preferreds have received, when the termination results wholly and directly

a foundation which is either legal, equitable or rational in any valid sense.

(2) These deficiencies are all the more apparent when it is considered that the asserted deprivation of the preferreds' "valuable" dividend rate was at best "theoretical", as Judge Leahy stated (note 31, *supra*), and in actual fact wholly *illusory*. For the "investment value ex the Act", determined by the preferreds' witness Badger and adopted by the Commission, not only did not represent values "apart from the Act" (since they depended upon and reflected such vital "Act" factors as the large retained earnings withheld from the common holders to provide for this liquidation required by the statute, as the Courts found,[32]) but neither were they in any legitimate connotation "*investment*" values at all.

Although this Court has cogently warned that "value is a word of many meanings",[33] it is difficult to conceive of a term less apt than that of "investment value" to characterize the results reached by the "valuation" process on

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from frustration of the enterprise by governmental edict" (District Court opinion, R. 291a; emphasis supplied).

Cf. Circuit Court opinion (R. 36):

"Under the plan the common stock is excluded from the holding company enterprise as effectively as are the preferred for the common under the plan will receive participation only in operating companies. *The fact is that the enterprise is at an end both for preferreds and common.* The Commission apparently has disregarded this fact which supplies the substantial differences between the instant case and the United Light & Power Company reorganization" (emphasis supplied).

[32] District Court (R. 306a, 469a-481a), Cf. Circuit Court (R. 37):

"The difficulty with the Commission's position in this connection * * * lies in the fact that while it has attempted to appraise the preferreds (as distinguished from the common) *ex* the Act, its basis for valuation, insofar as it has composed one, lies in factors which have come to existence because of the impact of the Act."

[33] Douglas, J., in *Group of Investors* v. *Milwaukee R. R.*, 318 U. S. 523, 540.

which the Commission here relied. That valuation process established nothing more than the fact that by reason of the unprecedentedly low money rates then prevailing as compared with the relatively high dividend rates which inferior grade holding company preferred stocks (such as Engineers admittedly were) have always necessarily borne, such stocks were momentarily selling at market prices in excess of their par or face amount.[34] Continuance of such market prices for any period in the future would depend predominantly upon the future level of basic money rates and yields for inferior grade preferred stocks of this type. The record of the proceedings before the Commission establishes that time and again witnesses emphasized that the then prevailing money rates primarily reflected artificial factors such as the Government's "pegging operations" which were subject to drastic revision at any time and ultimate abandonment; that the current stock market prices stood at post-war "boom" levels which could not be expected to prevail indefinitely, and especially so in the case of inferior grade preferred stocks such as those of Engineers; and that the future course of earnings of the system if permitted to remain in existence was fraught with many factors of a potentially adverse character. Finally it was emphasized that whereas developments of a favorable nature could not possibly enhance the "value" of the Engineers preferreds beyond the redemption prices, which imposed an absolute ceiling, unfavorable developments in any one of the elements above discussed would inevitably produce a decline in market price, the extent of which could be very large indeed, as the past history of the

[34] Thus, to the extent that Badger's report considered the investment characteristics of the Engineers preferreds, it showed them to be at best a low "medium grade" holding company preferred. But inasmuch as other inferior grade preferreds were currently selling at prices above par, Badger concluded that the Engineers preferreds would have a comparable market value as of that time (May, 1946). He acknowledged that such prices reflected primarily the unprecedentedly low money rates, which, in his opinion, were "permanent" (R. 1054a-1068a, 1085a-1086a). The sharp changes in money rates and preferred yields commenced shortly thereafter.

Engineers preferreds demonstrated (R. 522a-525a, 661a-674a, 1133a-1140a).[35]

The Commission completely ignored this testimony, and made no finding whatever either as to the future course of earnings or of money rates and yields relative to the Engineers preferreds if permitted to remain outstanding. Scarcely was the ink dry on the Commission's decision when market prices broke sharply, the "pegs" were lowered on Government securities, and interest rates and preferred stock yields commenced the sharp upward climb still in progress, and which has already reduced to below $100 the value the Engineers preferreds would have if outstanding (R. 122). Thus, while insisting that values must be determined "as though in a continuing enterprise" and "apart from the necessity for liquidation", the Commission *actually* valued the preferred stocks merely at the amount of their hypothetical market prices as of an assumed liquidation date. This paradoxical result not only demonstrates how misleading is the term "investment value ex the Act" to characterize the "values" determined for the Engineers preferreds, but also underscores the treacherous nature of the Commission's entire fictional doctrine. For the Commission was necessarily aware that if the Engineers plan related to the mere reorganization of a continuing enterprise, then values must be determined prospectively on a going-concern basis;[36] but although professing to adopt the fiction of a going concern *apart* from the neces-

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[35] As has been indicated, the Engineers preferreds sold as low as $10-$14 per share for all series during the depression years, and as recently as 1942 sold at $40-$47 per share (R. 1391a-1393a).

[36] Cf. *Consolidated Rock Products Co.* v. *Dubois*, 312 U. S. 510, 526; *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S. 523, 565-6; *Otis & Co.* v. *S. E. C.*, 323 U. S. 624, 632.

In other decisions the Commission has expressly recognized that values for reorganization purposes must be determined prospectively, and has rejected market values as a criterion. Thus in *Washington Ry. and Electric Co.*, Holding Company Act Release No. 7410 (May 1947), the Commission stated (p. 27): "However, we have never considered market values as determinative of the fairness of a Section 11(e) plan."

sity of liquidation, to the extent that it attempted to determine values (an attempt which was limited solely to the preferred stocks) the Commission contented itself with attempting to determine merely market values as of a particular moment preceding the final and complete liquidation which it recognized was in fact actually taking place.

B. Neither "the strict priority principle" nor the *Otis* decision furnish support for the Commission's rationale in the instant case.

(1) Petitioner's efforts to masquerade the Commission's "investment value ex the Act" doctrine in the guise of the strict priority principle and the *Otis* decision cannot withstand examination. *The strict priority principle is not at issue in this case.* From the outset, Engineers' plan by its very terms provided that the preferred stockholders would receive full payment of their entire claim in cash before the common stockholders would receive any participation. The basic issue at all times was the *amount* of that claim, and the mode of its determination. The Commission's view that the preferred stockholders should receive $3,200,000 in excess of the liquidation claim specified in the corporate charter surely finds no support in the bankruptcy and equity reorganization decisions which have enunciated the strict priority principle, since in such decisions the amount of the priority is invariably determined solely by reference to the contract provisions as embodied in charter or indenture. We are aware of no decisions, and Petitioners have referred to none, where it has been held that senior security holders in equity or bankruptcy reorganizations may validly receive amounts *in excess* of their contract claims.[37] By contrast, numerous are the

[37] Cf. Judge L. Hand, in *Knight* v. *Wertheim & Co.*: "We cannot agree that the debenture holders had as yet any legally protected interest in the property *beyond the principal and accrued interest of their bonds* which could be weighed against the shareholders' interest.

decisions holding that preferred stockholders are not entitled to receive their full liquidation claim where the reorganization takes the form of a merger or consolidation.[38] In *Otis & Co.* v. *S. E. C.*, 323 U. S. 624, this Court, with specific reference to "the devices of merger or consolidation" (p. 637), held that the mere reorganization and simplification of the *continuing* United Light holding company system proposed by the plan there under review would not be permitted to "mature" liquidation preferences merely because such reorganization had "as an incident to it the dissolution of *one company in a holding company system*".[39] To have permitted the preferred holders to demand immediate payment of their liquidation preference of $164 per share would have wiped out completely the common stockholders who concededly had a measurable interest in the continuing holding company enterprise, and would have bestowed a "windfall" on the preferred at the expense of the common.[40] Clearly this decision, which was expressly limited to the "narrow legal point" there involved,[41] furnishes no support for the contention that even

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If in fact they had relied upon sharing in an equity in the property above that amount, it was without warrant of law and constituted no reason for depriving the shareholders of whatever chance might remain of realizing upon their property." 158 F. 2d 838, 843; *cert. den. sub nom. McGuire* v. *Equitable Office Bldg. Corp.*, 331 U. S. 818. (Emphasis supplied.)

[38] Cf. *Chicago Corp.* v. *Munds*, 172 Atl. 452; *Root* v. *York Corp.*, 50 Atl. 2d 52; *American General Corp.* v. *Camp*, 190 Atl. 225, 230. In the decision last named, it was squarely held that premiums were not payable; and in *Matter of Fulton*, 257 N. Y. 487, the New York Court of Appeals reduced to $100 (the par value) the only instance disclosed by our research of an award in excess thereof.

[39] 323 U. S. 637. (Emphasis supplied.)

[40] "Enforcement of an overriding public policy should not have its effect visited on one class with a corresponding windfall to another class of security holders. * * * We must assume that Congress intended to exercise its power with the least possible harm to citizens" (323 U. S. 624, 637-8; emphasis supplied).

[41] 323 U. S. 624, 625.

in the case of simplification of a continuing enterprise in which retirement of preferred stocks is held necessary to comply with the Act, the preferred stockholders may demand cash payment not only of *the full matured liquidation claim* but also of substantial additional amounts.

But, above all, the *Otis* decision reflects the determination of this Court and the Courts below (the very ones which also passed on the case at bar) [42] to cut through surface technicalities and pierce to the substantive realities of the question. The very essence of the *Otis* decisions in all three Courts was the refusal to apply *liquidation* standards to a mere *simplification* and *reorganization* of a continuing holding company system.[43]. The Court's recent decision in *Schwabacher* v. *U. S.* was a reaffirmation of that same insistence upon dealing with realities by refusing to hold that matured liquidation claims were the measure of dissenting stockholders' rights in a *continuing* railroad enter-

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[42] Judge Leahy's opinion in the *United Light & Power (Otis)* case is reported at 51 F. Supp. 217, and that of the Circuit Court (per Judge Biggs) at 142 F. 2d 411.

[43] The Commission's brief in this Court in the *Otis* case strongly emphasized that a mere reorganization of a continuing holding company system was there involved, stating (p. 71):

> "Finally, in no realistic sense is there occurring *in this case* a dissolution of a business enterprise which should call for the application of a charter liquidation provision. As the opinion of the majority of the Commission discloses, the preferred and common stockholders of power have been the residual co-owners of a vast public-utility system controlled through Power, the top holding company, and Railways its principal *subholding company subsidiary*. These stockholders will continue to remain the residual owners *of the same public utility system.* * * * *In essence therefore, while Power is being dissolved the enterprise is not.*" (Emphasis supplied.)

Similarly, Professor Dodd, whose article is referred to in the majority opinion of this Court (p. 630) had repeatedly stressed the mere simplification of a continuing holding company system involved in the *United Light* case. Dodd, *Holding Company Act Recapitalizations* (1944), 57 Harv. L. Rev. 295, 308, 313.

prise augmented by merger.[44] Yet here Petitioners seek to rely on these decisions for justification in applying wholly *fictional* (and erroneous, as has been shown) *reorganization* standards to an incontestably authentic and final *liquidation*.

This Court's opinion in the *Otis* case pointed out (323 U. S. 632) that the Commission's findings there had correctly recognized and treated the United Light system as a continuing enterprise, had carefully estimated the system's future earning power, had determined that in approximately fifteen years the preferreds' dividend arrears would be entirely eliminated, and the common holders would thereafter have an interest of $2,858,000 annually in the earnings of the continuing system; and had embodied the respective claims of the preferred and common stockholders, as thus evaluated, in an allocation formula.[45] It is plain on its face that this process could have no valid application to the complete and final liquidation of the entire enterprise, as the Commission recognized in the instant case by not attempting to estimate future earning power or to evaluate the interests of the two classes of stockholders. Yet the Commission now asserts that the *Otis* decision requires the rights of the stockholders to be measured "as though the enterprise continues" *irrespec-*

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[44] "*Since the federal law clearly contemplates merger as a step in continuing the enterprise* it follows that what Michigan law might give these dissenters on *a winding up or liquidation* is irrelevant except insofar as it may be reflected in current values for which they are entitled to an equivalent. It would be inconsistent to allow state law to apply a liquidation basis to what federal law designates as a basis for continued public service" (*Schwabacher* v. *U. S.*, 334 U. S. 182, 200, emphasis supplied).

[45] It can be mathematically demonstrated that if the formula used in the *Otis* case to determine the respective rights of the preferred and common stockholders had been employed by the Commission in the instant case, the Engineers preferred stockholders would have received portfolio securities having a cash value of approximately $75 per share of preferred instead of the $100 cash actually paid to them.

tive of the fact that it does not;[46] and it further asserts that after measuring the rights of the preferred stockholders on this concededly fictional basis it need go no further because the common holders are merely entitled to receive whatever remains, *if anything*.

The cold, grim reality which confronts the common stockholders once the preferred have been generously treated on this fictional basis was recognized by both Courts below. In the instant case the existence of the redemption provision served to limit to $3,200,000 the premiums which the common holders were required to pay to the preferreds on this fictional hypothesis. But if the Engineers' preferreds were non-callable senior securities (such as are not unusual among utility holding companies),

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[46] It may be noted that certain of Petitioners apparently now seek to argue that the Engineers enterprise has not terminated because as an incident to the liquidation common stocks of three operating companies still owned by the holding company were distributed as a liquidating dividend to the Engineers common stockholders (for one of which the common stockholders paid $22,000,000 in cash). But, as this Court has had occasion to emphasize, a holding company is much more than a portfolio of securities: "North American is more than a mere investor in its subsidiaries" (*The North American Co. v. S. E. C.*, 327 U. S. 686, 701). It is axiomatic that the very essence of the holding company enterprise is concentrated control, accompanied by pyramiding and leverage (Cf. *American Power & Light Co. v. S. E. C.*, 329 U. S. 90). The dissolution of Engineers has wiped out all these along with the system, as concurrent findings of both Courts below establish.

Distribution of portfolio assets as a liquidating dividend is, of course, a normal incident of many corporate liquidations, and is in no sense distinguishable from total sale of the assets for cash and distribution of the latter. In fact, sales for cash were made by Engineers of virtually all of its assets other than the stock of these last three companies (as has been stated, the system comprised 17 electric, gas and transportation companies, in addition to holding companies, at the time the Act was passed). The substantial volume of sales on the Stock Exchange since the stocks of the three remaining subsidiaries were distributed establishes that many common stockholders have sold their stocks to obtain cash. Per contra, preferred holders who considered these stocks desirable, have been and are, in a position to purchase them freely on the Stock Exchange with the cash paid to them on retirement of the preferreds.

approximately $5,000,000 would have had to be paid on the basis of Badger's determination. And if a holding company has outstanding, as many do, bonds and several issues of non-callable preferred stocks, it is evident that virtually the entire equity of the common stockholders could be siphoned off in payment of the so-called "investment value" of the senior securities. In this way *little or nothing* might be left for common stocks possessed of substantial intrinsic value on both an asset and earning-power basis which, under all recognized reorganization principles, would ensure them large participations.

As Judge Leahy pointed out, such a doctrine is the *very antithesis* of the basic principle enunciated in the *Otis* decision, that "enforcement of an overriding public policy should not have its effect visited on one class with a corresponding windfall to another class of security holders" (323 U. S. 637).[47] The Circuit Court fully agreed that the Commission's one-sided fictional approach failed to achieve that "equitable" equivalence of the rights surrendered which is of the very essence of the *Otis* decision; but the Court bent over backwards to ensure the Commission virtually *untrammeled latitude* in the choice of techniques, so long as they are employed consistently and in a manner calculated to produce an equitable result.[48]

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[47] "The argument for payment of the premium is comparable to dealing cards off the top of a deck. When full hands (based on theoretical 'investment value') have been dealt to all the senior security holders, the common would merely get whatever happens to remain. Under the Act the interest of all investors must be considered. An emphasis on a preferred's rights must not slight the interests of the common. For if this occurs this is the direct opposite of the arguments utilized in United Light & Power *, * *" (R. 291a).

[48] "The selection of possible though varying techniques is for the Commission in the exercise of its expert administrative judgment. But whatever technique is chosen it must be employed consistently throughout the entire operation of valuation. We do not say the Commission must approach the problem of valuation *intra* the Act or *ex* the Act as the Commission purports to have done in the instant

Surely no Court could have gone further in yielding deference to the principle of administrative discretion, short of complete judicial abdication.

(2) In an effort to deflect attention from the palpable windfall which the Commission's decision bestowed upon the preferred holders at the expense of the common in contravention of the principles of the *Otis* case, Petitioners infer there are countervailing "economic benefits" which the common stockholders derived as the result of the forced retirement of the preferred.[49] The only basis suggested for this contention is a sentence in the Commission's opinion to the effect that "the retirement of the preferred stock will be of immediate benefit to the common stockholders" (R. 69a), a sentence which illuminates further the inconsistencies and paradoxes flowing from the Commission's fictional doctrine. For, examination of the context in which this statement appears makes it incontrovertibly plain that the Commission merely recognized that the impact of Section 11 on Engineers had been so severe, and the degree of governmental frustration of the enterprise so great, that the preferred stock had been transformed *as the result of the Act* into a burden for the common stockholders, instead of the valuable advantage it had formerly constituted and would at present constitute if not for the Act.[50]

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case. Either course consistently followed, could, we think, lead to just and appropriate valuations. No particular specific approach is to be nailed to the Commission's head. The Commission must, however, approach the problem of valuation with a full view of all the pertinent factors employing the same scales and the same measure throughout" (R. 37).

[49] Cf. Commission Petition, pp. 6, 17.

[50] The Commission's own words foreclose argument on this point. It stated (R. 59a):

> "The reduction of the Engineers holding company system from its previous size and diversity to a single operating company necessitates a commensurate contraction of its financial structure. Engineers' outstanding preferred instead of providing valuable leverage for the common, has become a burden."

Even in the face of the sacrifices and partial liquidation imposed on Engineers during the decade following passage of the Act, it would still have been highly advantageous to the common stockholders if they had been permitted to retain their enterprise alive and to continue the preferred stock outstanding.[51] But again the Act intervened to impose upon them the further and final requirement—the complete dissolution of the remainder of the enterprise. Under these circumstances, to refer to the "benefits" conferred by the Act upon the common by reason of the retirement of the preferred stock which the Act alone had transformed from a valuable asset into a burden (as the Commission itself stated) at best partakes of the character of an "exercise in semantics", as Judge Leahy aptly observed. [52]

IV. PETITIONERS' CONTENTIONS THAT THE COURT BELOW REQUIRED LOSSES TO BE "COMPUTED" AND "SHIFTED TO THE PREFERRED STOCKHOLDERS" ARE DEVOID OF MERIT.

Petitioners' contentions that the Commission is required by the opinions of the Court below to "compute" the losses sustained by Engineers in complying with the Commission's divestment orders and to "shift" such losses to the preferred stockholders [53] is a palpable misconstruction of

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[51] Many sound utility operating company stocks can be purchased at a price equal to 8 times current earnings, or equivalent to approximately 12½% on cost. If not for the Act, Engineers' common holders would have been free to retain the capital of the preferred holders without any limitations of time at an overall cost of approximately 5.40%, while realizing some 12½% upon this capital; or in the alternative, the common stockholders had the option of calling the preferred stock and replacing it with preferred carrying an even lower dividend rate (cf. Judge Leahy's finding, R. 311a-312a).

[52] R. 311a; quoted *in extenso* at p. 25 (note 27) of our cross-petition in No. 266.

[53] Commission Petition, p. 19; Streeter Petition, p. 35; Home Insurance Petition, p. 12.

the Court's holding on this subject. Since it was the theory of the Commission that the preferred stockholders were entitled to receive premiums based on valuations "*ex* the Act", it was unquestionably pertinent to point out that for more than ten years there *had been* such an Act, and that the common stockholders had sustained many losses and deprivations in the process of complying with it. No suggestion was made that the preferred stockholders should share these losses and deprivations, but merely that they should not be permitted to impose additional ones by demanding payment of a $3,200,000 bonus on the theory that the existence of the Act and its requirement for complete liquidation should now be ignored.

The record establishes, and the Courts found, that for the common stockholders the Act had been an unblinkable reality indeed. Yet the common stockholders had at all times safeguarded the preferred against the slightest loss, and had met their obligations to the preferred meticulously and promptly, except for a short period of dividend arrears, which was quickly thereafter compensated. In consequence, the preferred stockholders have been paid every dollar promised to them, and have received in the aggregate approximately $190 for every $100 (or less) which they or their predecessors invested in the enterprise.[54] But when it was contended that "fairness and equity" require that the contract limitations be disregarded and that the preferred stockholders be paid an additional $3,200,000 for the theoretical *future* deprivation of their lucrative dividend rate, surely it was relevant on the basis of every equitable consideration for courts of equity to insist that some consideration also be given *at this stage* to the deprivations of the common. When courts are urged to

[54] R. 303a. The common stockholders, on the other hand, after having gone without any dividends continuously for some 16 years, realized in the liquidation an amount barely approximating the average sum actually received by the Company for the common stock, and equal to only 40% of the prices paid by common stockholders who purchased at the market high in pre-depression years (R. 305a).

disregard contractual limitations in order to reach results alleged to be *more equitable*, they can scarcely be asked to function with one eye blindfolded and the other half shut. Only recently Mr. Justice Murphy had occasion to emphasize this principle in the context of a corporate reorganization, stating, "*Equity looks in all directions.* Only in that way can the various interests in the corporate community be adequately protected." [55]

In like manner, courts of equity could not countenance the appropriation for the benefit of the preferred, in valuing them allegedly *ex* the Act, of the more than $24,000,000 of earnings which accrued to the equity of the common stockholders and were left in the enterprise in order to provide for the liquidation compelled by this very Act.[56] These earnings of the common stockholders thus having accrued while Engineers was in effect in *custodia legis*, it would be even less fair and equitable to add them to the "value" of the preferred stocks upon which the common stockholders are then required to pay premiums than was the claim for double interest which was disallowed in *Vanston Bondholder's Committee* v. *Green*, where Mr. Justice Black stated for the Court: "Such a result is not consistent with equitable principles." [57]

Petitioners' arguments that the Commission is required to undertake the onerous task of "computing" losses and "reconstructing the enterprise" rest upon an overly ingenuous interpretation of the Circuit Court's language. The Court did *not* state that such items must be "computed", but merely that they must be "*weighed into the calculation*"; a phrase which, along with the term "bookkeeping", was obviously intended figuratively and not

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[55] *Comstock* v. *Group of Institutional Investors*, 335 U. S. 211, 238. (Emphasis supplied.)

[56] District Court Findings Nos. 34, 35, 36, 47 (R. 306a, 307a, 312a). Cf. Circuit Court Opinion (R. 37).

[57] 329 U. S. 156, 167.

literally.[58] It is thus evident that the Court had no intention of insisting upon the exact ascertainment and computation of each loss sustained by Engineers, but merely upon giving reasonable consideration to the fact that such losses (without necessity for precise computation) had been sustained. Moreover, the Court emphasized that even this relatively simple task was not mandatory upon the Commission unless it elected to determine values "ex the impact of the Act"; in such event, the Court held,[59] logic and consistency would be violated if the Commission took into consideration in valuing only *the senior securities* "ex the impact of the Act", favorable factors created by the deprivations and sacrifices imposed upon the common stockholders by this very same Act.

It is particularly significant, in the light of Petitioners' plaints as to the legal irrelevance and administrative impracticability of according consideration to such factors as the issue price, past market history and low investment rating of the preferreds that for a period of some five years the Commission's decisions consistently accorded such factors detailed consideration; indeed, they accorded such factors virtually controlling weight.[60] Nor is there room for an argument that these decisions were superseded by the *Otis* decisions, since many of them were issued by the Commission subsequently. Thus, for example, in the *Interstate Power Company* decision, submitted to Judge Leahy for enforcement only a few weeks prior to the *Engineers* plan, the Commission held that owners of *first mortgage 5% bonds* of a public utility operating company were entitled to receive only the par value, *notwithstand-*

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[58] "* * * if the equitable equivalents for relinquished securities are to be arrived at by the Commission under the doctrine of the *Otis & Co.* case, ex the Act, losses of the sort referred to in this paragraph must *be weighed into the calculation*, i.e., such losses should be returned to the credit side of the enterprise's balance sheet as a matter of bookkeeping" (R. 37; emphasis supplied).

[59] See note 48, *supra*.

[60] See the non-premium decisions discussed *supra*, pp. 17-19.

ing that the bonds had been selling at a premium of 3½ points above par, the Commission stating:

> "The bonds were originally sold to the public in 1927, 1928 and 1931 at prices of 97½, 96 and 93 respectively. During most of the years since issuance, the bonds have sold on the market at prices substantially less than par; indeed the bonds never sold as high as par until 1945. In 1937 the bonds sold as low as 32; and as recently as 1940 they sold at a low of 51½. At original issuance and sale of the bonds in 1927, a rating A was assigned them by *Moody's Investors Service,* Standard Statistics rated them B1+. In following years, both ratings were successively lowered to a Moody's rating of B in 1938, and all subsequent years, and a Standard's rating of C1+ in 1940 and all subsequent years." [61]

Yet *the very same factors* pointing to an *even more speculative caliber for the Engineers preferreds* [62] were wholly

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[61] *Interstate Power Company,* Holding Company Act Release No. 7143 (Jan., 1947), approved and enforced 71 F. Supp. 164 (D. C., Del., 1947); cf. also recent decisions in *Republic Service Company,* Holding Company Act Release No. 8170 (April 30, 1948) and *Lehigh Valley Transit Company,* Holding Company Act Release No. 8445 (August 18, 1948), in which the Commission held that payment of par without premiums was fair and equitable to debenture holders, emphasizing their past market history and original issue prices and deeming irrelevant the 9 point premium at which the *Lehigh* bonds had sold in recent years.

[62] Thus, in order to sell the Engineers $5 and $5.50 preferreds in 1928 at prices comparable to those of the Interstate Bonds, it was necessary to attach warrants and conversion rights (since expired) having a substantial independent value. The Interstate Bonds were never in default of interest; the Engineers preferreds were in arrears of dividends over a period of four years, during most of which the dividends were not even earned. The Engineers preferreds sold as low as $10 per share in 1933, as low as $14 per share in 1935; and as recently as 1942 sold as low as $40-$47 per share (R. 1391a-1393a). They never attained par until 1944, when large scale market purchases by Engineers forced them up. Standard & Poor's Investment Service rated them C** at the end of 1944 (the last year in which it rated preferred stocks), which rating was defined as "Preferred stocks with erratic dividend records, and which can be expected to make payments only under favorable conditions" (R. 1844a).

ignored by the Commission in its decision; and Petitioners now seek to contend that the Courts below have imposed upon the Commission a legally irrelevant and administratively onerous task in requiring such factors to be considered.

CONCLUSION

The sharp upward revisions which have taken place in interest rates and preferred stock yields subsequent to the date of the testimony relied upon by the Commission in determining the so-called "investment value" of the Engineers preferred stocks foreclose the possibility that any amounts may be found payable, beyond those already paid, pursuant to the decree of the District Court, even if Petitioners were to be upheld in their contentions that the Commission's rationale was valid and the holdings of the Court below were wrong on every issue. However, the Circuit Court's decision was entirely correct on the merits, for all the reasons hereinabove stated, except in requiring the remand to the Commission. By reason of the remand, there is as yet no final determination of basic issues or of the rights of the parties.

The petitions for certiorari should be denied. If, however, the Court concludes otherwise, our cross-petition (No. 266) should also be granted.

Dated: September 20, 1948.

Respectfully submitted,

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APPENDIX

Sections 11(e) and 24(a) of the Public Utility Holding Company Act of 1935, 49 Stat. 803, 15 U. S. C. 79a et seq. provide as follows:

"SECTION 11(e): In accordance with such rules and regulations or order as the Commission may deem necessary or appropriate in the public interest or for the protection of investors or consumers, any registered holding company or any subsidiary company of a registered holding company may, at any time after January 1, 1936, submit a plan to the Commission for the divestment of control, securities, or other assets, or for other action by such company or any subsidiary company thereof for the purpose of enabling such company or any subsidiary company thereof to comply with the provisions of subsection (b). If after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, the Commission shall make an order approving such plan; and the Commission, at the request of the company, may apply to a court, in accordance with the provisions of subsection (f) of section 18, to enforce and carry out the terms and provisions of such plan. If, upon any such application, the court, after notice and opportunity for hearing, shall approve such plan as fair and equitable and as appropriate to effectuate the provisions of section 11, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer, under the direction of the court and in accordance with the plan theretofore approved by the court and the Commission, the assets so possessed."

"SECTION 24(a): Any person or party aggrieved by an order issued by the Commission under this title may

obtain a review of such order in the circuit court of appeals of the United States within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith served upon any member of the Commission, or upon any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall certify and file in the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence, and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the Court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347)."